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IN THE

# SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1973

No. 73-1291

ROBERT B. BRUCE,
Petitioner,

vs.

UNITED STATES OF AMERICA,
Respondent.

## PETITION FOR A WRIT OF CERTIORARI

**To the United States Court of Appeals for the Fifth Circuit**

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**To the United States Court of Appeals for the Fifth Circuit**

Robert B. Bruce, your petitioner, prays that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals for the Fifth Circuit entered in the above entitled case December 18, 1973. A petition for rehearing was denied January 25, 1974.

### OPINION BELOW

The opinion of the Court of Appeals has not been reported. A copy is appended as Appendix I.

## JURISDICTION

The judgment of the Court of Appeals was entered December 18, 1973. Petition for rehearing was denied January 25, 1974.

Jurisdiction to issue the writ is invoked, pursuant to the provisions of Title 28, Section 1254 (1), United States Code.

Petitioner was convicted in the United States District Court for the Northern District of Georgia on two counts of a multi-count indictment charging him with violations of the provisions of **Title 18, Section 1341, United States Code,** and **Title 18, Section 371, United States Code.**

## QUESTIONS PRESENTED

1. Whether the definition of fraud announced by the Fifth Circuit Court of Appeals in its decision in **Gregory v. United States,** 5 Cir., 253 F2d 104, 109, viz:

> "Essentially, a scheme to defraud is measured by a non-technical standard. 'It is a reflection of moral uprightness, of fundamental honesty, fair play and right dealing in the general and business life of members of society.' "

was properly applied to a criminal prosecution involving violations of the Federal Securities Act (**Title 15, Section 77q** (a), et seq., United States Code)?

2. Whether the offer and sale of securities issued by an insolvent corporation, utilizing prospectuses which show the corporation to be insolvent, constitute offenses punishable under the Federal Securities Act (**Title 15, Section 77q (a),** et seq., United States Code)?

3. Whether Petitioner, by reason of the failure of the Fifth Circuit Court of Appeals to consider and rule on the errors assigned by him in his Appeal, has been denied procedural safeguards established for the protection of person charged with criminal offenses and thereby denied due process of law?

## CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

The Fifth Amendment to the Constitution of the United States Provides:

> "No person shall . . . be deprived of life, liberty or property, without due process of law; . . ."

**Title 15, Section 77q (a), United States Code** provides:

> "It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly—
>
> (1) To employ any device, scheme, or artifice to defraud, or
>
> (2) To obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser."

**Title 18, Section 1341, United States Code,** provides:

> "Whoever, having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or

property by means of false or fraudulent pretenses, representations, or promises, or to sell, dispose of, loan, exchange, alter, give away, distribute, supply, or furnish or procure for unlawful use any counterfeit or spurious coin, obligation, security, or other article, or anything represented to be or intimated or held out to be such counterfeit or spurious article, for the purpose of executing such scheme or artifice or attempting so to do, places in any post office or authorized depository for mail matter, any matter or thing whatever to be sent or delivered by the Post Office Department, or takes or receives therefrom, any such matter or thing, or knowingly causes to be delivered by mail according to the direction thereon, or at a place at which it is directed to be delivered by the person to whom it is addressed, any such matter or thing, shall be fined not more than $1,000, or imprisoned not more than five years, or both."

**Title 18, Section 371, United States Code** Provides:

"If two or more persons conspire either to commit any offense against the United States, or to defraud the United States, or any agency thereof in any manner or for any purpose, and one or more of such persons do any act to effect the object of the conspiracy, each shall be fined not more than $10,000 or imprisoned not more than five years, or both.

If, however, the offense, the commission of which is the object of the conspiracy, is a misdemeanor only, the punishment for such conspiracy shall not exceed the maximum punishment provided for such misdemeanor."

## STATEMENT OF THE CASE

Petitioner, along with Robert S. Walker and Robert A. Blackwood, was charged in a multi-count indictment in the Atlanta Division of the Northern District of Georgia with violations of the Securities Act (Title 15, Section 77q (a) USC), Mail Fraud (Title 18, Section 1341, USC), and Conspiracy (Title 18, Section 371, USC).

A jury trial was waived and, following a lengthy trial to the Court, a verdict was entered finding him guilty on two counts (mail fraud and conspiracy). Thereafter, concurrent sentences of two years on each count, to serve six (6) months in a jail type institution, the remainder to be suspended, were imposed. Copy of the amended verdict is appended as Appendix II.

The violations are charged to have occurred with respect to American Capital Corporation, a Georgia Corporation, of which defendant Robert S. Walker was President, defendant Robert A. Blackwood was Secretary from its inception until about November, 1967, and John R. Creighton Secretary thereafter.

American Capital began operations about December 13, 1966, and ceased approximately April 30, 1969. A total of $61,055 is alleged by the Government to have been received from sales of stock, which included $25,000 from initial stockholders and $154,367 from issuance of investment certificates. The first investment certificate was sold May, 1967, and the last in March, 1969. Total cash received was $215,960.84.

Appellant Bruce is from Miami, Florida, and is an accountant and management consultant. He was contacted by Appellant Walker in December, 1966, to perform an audit for use in filing an intrastate registration in Georgia. Thereafter, Bruce prepared the financial statements incorporated in the American

Capital prospectus dated January 31, 1967, and a second prospectus dated April 5, 1968.

The prospectuses carried boldly announced investment admonitions, viz:

> "THESE ARE SPECULATIVE SECURITIES
>
> 'This is not to be construed as a guarantee that there will be profits made by the Company, but is only a guarantee that when and if such profits are made, the stated percentage thereof will be paid to the holders of these Investment Certificates.
>
> Except as otherwise indicated, this Prospectus speaks as of its date of issue.' Neither the delivery hereof, nor any sale made hereunder, shall create an implication that the affairs of the Company have continued without change since said date.' "

Bruce was never an officer or stockholder of American Capital, at any time, solicited no sales, and received only a total of $1800.00, plus some expenses, as remuneration for all accounting services performed.

George M. Callahan, an employee of the Securities and Exchange Commission, was utilized by the Government as an expert. Callahan considered the company insolvent as of May, 1967. Approximately $166,000 was received from the sale of stocks and investment certificates after that time.

Callahan characterized the financial statements prepared by Bruce as not in keeping with sound accounting principles. In the first prospectus his criticisms in the main were levelled, viz:

(a) Inclusion of a note of Robert A. Blackwood for the principal sum of $20,000, secured by 40,000 shares of American Capital Stock (with a legend entered on

the reverse side thereof attempting to limit liability to the stock itself) as a "note receivable"; and

(b) Utilizing an MAI appraisal of Florida real estate at valuation of $1,076,600, rather than $380,387.74, its theoretical cost to the company, in arriving at net worth.

As to the second prospectus, Callahan voiced criticisms, viz:

(a) Cash in bank of $40,000 should not have been included because it represented a savings account being held as collateral for a bank loan in equal amount, the loan being listed as a liability;

(b) The Florida land, although shown as having been foreclosed on, nevertheless was mentioned as a proposed reacquisition, and he considered it improper to state a deficit position and then project hopes, which if fulfilled, would make it solvent again; and

(c) Inclusion of unaudited net worth of Babee-Tenda Products Corporation as of February 16, 1968, of $289,000 since, in his view, mention of unaudited figures with audited figures would thereby give credence to the unaudited.

No witness called by the Government during the lengthy trial testified that either prospectus was relied on in making an investment in American Capital Corporation.

## REASONS FOR GRANTING THE WRIT

I. The Fifth Circuit Court of Appeals, by its decision in the instant case, has announced a new and far-reaching test of criminality in Federal fraud prosecutions, viz:

> "Essentially, a scheme to defraud is measured by a non-technical standard. 'It is a reflection of moral uprightness, of fundamental honesty, fair play and right dealing in the general and business life of members of society.'
>
> **Gregory v. United States,** 5 Cir., 1958, 253 F2d 104, 109"

This definition authorizes a finding of guilt upon the fact finder's notions of "moral uprightness", "fundamental honesty", "fair play", and "right dealing."

II. The Fifth Circuit Court of Appeals, by its decision in the instant case, has announced the principle that the offering for sale of securities in an insolvent company violates the Federal Securities Act, even though the prospectus clearly shows the company to be insolvent.

III. The Fifth Circuit Court of Appeals, by its decision herein, ignored and failed to pass upon errors assigned by petitioner in his appeal and thereby denied him the procedural safe-guards guaranteed by the Fifth Amendment.

### I

### A New Definition of Fraud

The decision of the Fifth Circuit announces a new approach to fraud cases which greatly expands the scope of Federal intervention in everyday business transactions. The test for determining what constitutes a federally proscribed criminal fraud is especially far-reaching: "Essentially, a scheme to defraud is measured by a non-technical standard. 'It is a reflection of

moral uprightness, of fundamental honesty, fair play and right dealing in the general and business life of members of society', Gregory v. United States, 5 Cir., 1958, 253 F2d 104, 109." Slip Op. at p. 12. The Court then continues to state that a scheme to defraud need not even be fraudulent or misrepresent any material fact to be a violation of federal law, if persons of ordinary prudence and comprehension could be misled as to the **possible** future value of an investment in a particular business endeavor.

In the Fifth Judicial Circuit fraud cases will now be equated with obscenity cases. Criminality will be determined not by whether there was an intent to obtain money or property through false pretenses (or failure to disclose material facts), but rather, whether the course of business dealings of the particular defendant comports with the community's ideals of "moral uprightness, of fundamental honesty, fair play and right dealing."

If the fact finder, jury or as here, District Judge, considers the particular defendant to have violated prevailing community standards of "moral uprightness, of fundamental honesty, fair play and right dealing", i.e., transgressed the morals of the local market place, and made an incidental use of the mails in connection therewith, a Federal crime will be found to have been committed. This could mean one thing in New York, another in Georgia, and something else in California.

The Court did not stop here, however, but continued:

> "The scheme need not be fraudulent upon its face or misrepresent any material fact. All that is necessary is that it be a scheme reasonably calculated to deceive persons of ordinary prudence and comprehension."

The statutes themselves, **Title 15, Section 77q(a),** and **Title 18, Section 1341,** are more narrowly drawn, and should not be thus watered down.

## II

### Sales of Securities in an Insolvent Corporation

The Fifth Circuit Court of Appeals has announced, and as a holding of first impression, that the offering of securities issued by an insolvent company violates the Federal Securities Acts, even though the prospectus discloses the fact of insolvency clearly.

This case was prosecuted by the Government under the theory that the prospectuses of the company were false and misleading. Yet the District Court found defendants guilty, and the Court of Appeals upheld same for an entirely opposite and novel reason—although both Courts agreed that the prospectus **on its face** clearly showed the company to be financially insolvent, the Defendants were guilty of fraud for continuing to offer such securities for sale, because the prospectus disclosed that the company could not succeed. The Courts reasoned that the Defendants must have known that the company was insolvent because the prospectus clearly demonstrated its dire financial condition. Nevertheless, the Defendants continued to offer these securities to those who desired to risk an investment in an admittedly financially questionable enterprise.

If such activity constitutes a violation of Federal securities laws and the mail fraud statute, then every person offering securities in a financially t[illegible]led business which ultimately fails faces the prospect of federal prosecution. The venture must succeed if the offeror is to escape criminal sanctions.

## III

### Petitioner Has Been Denied Due Process of Law

In his appeal petitioner assigned procedural errors committed by the District Judge which were substantial in nature and deprived him of a fair trial, viz:

1. The Court erred in permitting G. M. Callahan, an employee of the SEC, to qualify as an expert, and thereafter testify to "generally accepted accounting procedures," and he had not engaged in the practice of public accounting since 1947.

**Shreve v. United States,** 9 Cir., 103 F2d 796;

**Fineberg v. United States,** 9 Cir., 393 F2d 417, 421.

2. The Court erred in requiring Appellant Bruce to answer he had been de-certified as a public accountant by the State of Florida, this being irrelevant to the issues of the case and prejudiced him in the eyes of the Court.

**Piassick v. United States,** 5 Cir., 253 F2d 658;

**Colorificia Italiano Max Mayer, etc. v. S/S Hellenic Wave, etc.,** 5 Cir., 419 F2d 223.

3. The Court erroneously failed to grant Appellant's Motion for Judgment of Acquittal and erred in thereafter adjudging him guilty on Counts Nine and Fifteen. In so doing, Appellant stands convicted on the notions of Government Witness Callahan with respect to "generally accepted accounting procedures" in the preparation of financial statements incorporated in the first and second prospectus issued by American Capital Corporation, which views were as a matter of law inaccurate in that

(a) The Blackwood note was a valid and binding obligation under applicable Georgia Law.

**Farkas v. Farkas,** Trustee, 200 Ga. 886, 38 S.E. 2d 924;

**Fouche v. Merchants National Bank of Rome,** 110 Ga. 827, 841, 36 S.E. 256;

**Spratling v. Westbrook,** 140 Ga. 625, 79 S.E. 536;

**Adcock, Administratrix v. Mandeville Mills,** 182 Ga. 244, 185 S.E. 288;

**Citizens and Southern National Bank v. Johnson,** 214 Ga. 229, 104 S.E.2d 123.

(b) The MAI appraisal, stating a value of $1,076,600 for the Florida land, was property utilized under expert testimony offered by Appellant, and the accuracy of this valuation was verified by Henry Blanton, a Florida Realtor familiar with the property, who testified as a witness in the case.

**Beardsley v. Ernst,** 47 Ohio App. 241, 16 Ohio L. Abs. 719, 191 N.E. 808.

(c) Inclusion of the unaudited net worth of Babee Tenda Products was appropriate since the figure stated was carefully labeled "unaudited".

**Stephens Industries, Inc. v. Haskins and Sells,** 10 Cir., 438 F.2d 357.

(d) The pledged savings account at First Bank of Palmetto, Georgia, was not inaccurately included in the financial statement but its status as collateral to the company's note, and the fact that it had been used to satisfy the note on March 16, 1968, was clearly stated in the footnote.

**O'Conner v. Ludlam,** 2 Cir., 92 F.2d 50, cer den 302 U.S. 758, 82 L.Ed. 586, 58 S. Ct. 364.

(e) Reporting the foreclosure proceeds against the Florida land with resultant net loss of $693,196.50 for the period January 1 to February 13, 1968, a deficit net worth of $89,005.33 and a net deficit of $112,452.63, was a correct statement of fact. Noting the existence of an option to redeem by payment of $300,000 could not be fraud on the part of Appellant.

**O'Conner v. Ludlam,** 2 Cir., 92 F.2d 50, 56, supra.

In its lengthy, and rather generalized opinion, the Fifth Circuit Court of Appeals failed to consider and rule upon the

errors so assigned. Thereby, petitioner has been denied due process of law and deprived of his rights under the Fifth Amendment.

Respectfully submitted

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